



STATE OF CALIFORNIA
FRANCHISE TAX BOARD - LEGAL DEPARTMENT
PO Box 1720
Rancho Cordova CA 95741-1720

STEVE WESTLY
Chair

CAROLE MIGDEN
Member

MICHAEL C. GENEST
Member

MEMORANDUM

TO: EXEMPT ORGANIZATIONS UNIT
BUSINESS ENTITIES SECTION

Date: January 21, 2005
Case: 1020249210183006
Case Unit: 1020249210183010
Technical Advice Memorandum 2005-0002

FROM: EDWARD J. KLINE

RE: Review of the California Corporations Code

QUESTION PRESENTED

You have requested an opinion regarding the requirement, if any, for the Exempt Organizations Unit to review and consider California Nonprofit Corporation Law¹ provisions during the review of Exempt Applications.

CONCLUSIONS

The Secretary of State is the correct California agency to review articles of incorporation for conformity to the Nonprofit Corporation Law.² Because the staff of the Secretary of State enforces these portions of the Corporations Code, and to avoid any conflicts resulting from different interpretations of the Nonprofit Corporation Law, it is appropriate for the staff of the Franchise Tax Board to defer to the judgment of the staff of the Secretary of State regarding articles of incorporation and compliance with Nonprofit Corporations Law provisions.³

¹ California Corp. Code section 5000 et seq, which includes both the Nonprofit Public Benefit Corporation Law and the Nonprofit Mutual Benefit Corporation law.

² Corp. Code section 5008. (a) Upon receipt of any instrument by the Secretary of State for filing pursuant to this part, Part 2, Part 3, Part 4 or Part 5, if it conforms to law, it shall be filed by, and in the office of the Secretary of State and the date of filing endorsed thereon.

³ I have personal knowledge of two examples of applications for exemption with provisions that appeared to disqualify the organization under the Nonprofit Mutual Benefit Corporation Law. In both cases the staff of the Secretary of State interpreted these sections differently, concluded the organizations did qualify under the Nonprofit Mutual Benefit Corporation Law, and staff of the Franchise Tax Board deferred to the judgment of the staff of the Secretary of State.

Staff of the Franchise Tax Board does however, have the authority and responsibility to ensure compliance with provisions of the Revenue and Taxation Code as part of the review of Exempt Applications.⁴

BACKGROUND

During the late 1970s, the Nonprofit Corporation Law was subject to a major revision and rewrite, with an effective date of January 1, 1980. As a result of the changes to the Nonprofit Corporation Law, and specifically section 5227⁵, the Manager of the Exempt Organization Section requested an opinion from the Chief Counsel regarding the effect of a violation of section 5227 on an application for exemption from franchise and income tax. In reply, on May 19, 1980, the Chief Counsel opined that failure to comply with Corporations Code section 5227 was sufficient reason to deny exemption under Revenue and Taxation Code. The opinion was to be applied prospectively and there were a number of qualifications in the opinion.⁶

Based on the information provided with the Exemption Application, staff of the Exempt Organizations Unit has identified a number of other sections of the Nonprofit Corporation Law Code that appear to disqualify an organization from qualifying as a Nonprofit Public Benefit Corporation or Nonprofit Mutual Benefit Corporation. The articles of incorporation for these organizations have been approved and endorsed by the Secretary of State.

ANALYSIS AND DISCUSSION

The Secretary of State reviews articles of incorporation and applications for incorporation for compliance under the Nonprofit Corporation Law, and if acceptable files and endorses the articles of incorporation. This review includes applications for incorporation as a Nonprofit Public Benefit Corporation (Corp. Code section 5110 et seq.) or a Nonprofit Mutual Benefit Corporation (Corp. Code section 7110 et seq.) Staff of the Secretary of State has stated that a further review by FTB staff for the correct application of the Corporations Code to organizations applying for exemption from franchise tax is not considered necessary or warranted.⁷

⁴ Rev. & Tax. Code section 19501. The Franchise Tax Board shall administer and enforce Part 10 (commencing with Section 17001), Part 10.7 (commencing with Section 21001), Part 11 (commencing with Section 23001), and this part [Part 10.2.]

⁵ Corp. Code section 5227. (a) Any other provision of this part notwithstanding, not more than 49 percent of the persons serving on the board of any corporation may be interested persons.

⁶ Because Corp. Code section 200 allows a corporation to be formed by one or more persons, the requirements of section 5227 are no longer considered significant.

⁷ Supervising Counsel Betsy Bogart, Secretary of State, at a joint staff meeting of the Franchise Tax Board and Secretary of State on June 16, 2004.

January 21, 2005

Regarding compliance with the Nonprofit Corporation Law, staff of the Exempt Organizations Unit has deferred to the staff of the Secretary of State regarding the form and language of the sample articles of incorporation included with the Exempt Application, FTB Form 3500.

SUMMARY

The Secretary of State is the correct California agency to review articles of incorporation for compliance with the Nonprofit Corporation Law and it is not considered necessary or appropriate for FTB staff to further review articles of incorporation for conformity to the Nonprofit Corporation Law.

Tax Counsel IV
Telephone: (916) 845-5087
FAX: (916) 843-6034

cc: